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c/o

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Dear Sirs/Mesdames:

**CSA Consultation Paper 92-401 – *Derivatives Trading Facilities***

This letter is in response to the request for comments regarding the above-noted CSA Consultation Paper (the “**Consultation Paper**”). As counsel to global financial institutions, pension plans, commodity producers, investment funds and derivatives trading platforms, Osler has extensive involvement with derivatives transactions and derivatives regulation. This comment letter is also informed by input from clients that trade derivatives or that would be subject to regulation as derivatives trading facilities (a “**DTF**”). We have responded to a selection of the questions posed by the CSA Derivatives Committee (the “**Committee**”) in the Consultation Paper that are most relevant to our clients.

*1. Is the DTF category appropriately defined? If not, what changes are needed and why?*

In our view, the DTF category is appropriately defined. The definition is flexible and takes into account a variety of trading platforms and execution methods. We are also supportive of the enumerated exclusions from the DTF definition. In particular, we think that it is appropriate to exclude: (i) purely bilateral trading, (ii) one-to-many facilities such as single-dealer platforms and (iii) facilities or processes where there is no actual trade execution or arranging taking place, such as bulletin boards, electronic post-trade confirmation services and portfolio compression services. For example, portfolio

compression service providers such as TriOptima, Creditex and Markit should not be subject to DTF regulation in Canada. We recommend that these exclusions should be included in companion policy guidance that accompanies any future DTF rules.

*4. Please comment on required modes of execution. Should any particular minimum trading functionality be prescribed for DTFs generally?*

In our view, there should be no minimum trading functionality prescribed for DTFs. If an entity satisfies the definition of DTF by virtue of the modes of execution it makes available to Canadian participants, then it will need to be regulated as a DTF but should not be required to add modes of execution to its facility. For example, it would not be appropriate to require a small DTF that offers RFQ functionality in a particular asset class to also offer a central limit order book (“**CLOB**”), particularly if that asset class is not well-suited to trading via a CLOB.

Also, we note that the request-for-stream execution method would depend on market makers to provide continuous streaming quotes. It would be helpful for the Committee to define market making activity in the context of request-for-stream execution methods, and whether such activity would be considered to be the business of dealing in derivatives as a dealer under futures derivatives registration rules, particularly if the market maker is located outside of Canada and provides market-making services only on foreign-based DTFs.

*5. Is the proposed regulatory framework for DTFs appropriate?*

The proposed regulatory framework for DTFs is appropriate. We applaud the Committee for stating the intention to regulate DTFs under new rules appropriate for derivatives trading, and to not regulate DTFs under the existing regulatory framework for securities and futures exchanges, ATs and QTRSs in NI 21-101.

Also, it is appropriate for the Committee to recommend that DTFs may be authorized or exempt from authorization. We are supportive of the proposal to grant exemptive relief to foreign-based DTFs that are subject to comparable regulation in their home jurisdictions. Given the cross-border nature of derivatives trading, it is important to support harmonized rule making, substituted compliance and regulatory reciprocity wherever possible.

Finally, we encourage the Committee to follow a principles-based approach to regulation of DTFs. A principles-based approach will encourage effective regulatory oversight while preserving needed flexibility for DTFs to operate their businesses in a dynamic and competitive market.

6. *Is it appropriate to impose dealer requirements on a DTF where the operator of the DTF exercises discretion in the execution of transactions? (Please explain.) If so, should such a DTF be required to register as a dealer, or should only certain dealer requirements be imposed on the DTF? (Which ones?)*

Without a derivatives dealer registration regime in Canada, it is not possible to comment on the possible application of dealer requirements on a DTF that exercises discretion. The requirements of a derivatives dealer regime may be unduly onerous for a DTF. For example, in our view it would not be appropriate to require that a DTF become a member of IIROC simply because it exercises discretion in the execution of transactions.

There are many alternatives for regulating DTFs that exercise discretion, such as specific business conduct requirements in the future DTF rule. The Committee should adopt a flexible approach to regulating DTFs that exercise discretion. It may be necessary and valuable to Canadian derivatives markets to permit a DTF to exercise discretion, particularly if the DTF facilitates trading of bespoke derivatives that may not otherwise be suitable for electronic trading. Regulation of DTFs that exercise discretion must be appropriately balanced between limiting the potential for conflicts of interest and permitting worthwhile activity.

7. *To address conflicts of interest, should a DTF that exercises discretion in the execution of transactions be required to exercise this functionality in a separate affiliated entity? Why or why not?*

No, a DTF that exercises discretion in the execution of transactions should not be required to exercise this functionality in a separate affiliated entity. Requiring the functionality in a separate affiliated entity would be unnecessarily costly and burdensome. Consider the example of securities marketplace regulation, where there are examples of firms carrying on business as a brokerage firm and an ATS out of the same entity (with appropriate policies and procedures to manage against conflicts of interest). Similar requirements should be adopted for DTFs that exercise discretion.

8. *What factors are relevant in defining the proposed best execution duty?*

Any duty of best execution of a DTF that exercises discretion in respect of derivatives trading should be clearly distinguished from best execution in respect of securities trading. Given the unique characteristics of derivatives products and various execution methods, even if traded on a DTF, a best execution duty may be very difficult to define and enforce. Further study and harmonization with international approaches is necessary.

10. *Is it appropriate to allow a DTF to require transactions executed on its facility to be cleared through a particular clearing agency and/or reported to a particular trade repository?*

Should it be decided that DTFs must engage in trade reporting to trade repositories, then a DTF should have the right to choose the trade repository to which it will report (assuming that the repository is appropriately recognized in the Canadian jurisdiction).

We also note that a DTF should not be required to provide access and trading feeds to all regulated clearing agencies. A DTF should have the right to choose to connect to certain clearing agencies and not others. If a DTF does not connect to a particular clearing agency that is preferred by a participant, then that participant is free to trade on other DTFs that connect to the preferred clearing agency. However, if a DTF connects to multiple clearing agencies, then participants should have the right to choose the clearing agency they wish to use to clear a transaction.

*11. Is it appropriate for a DTF that exercises discretion in trade execution to be permitted to limit access to its facility? If so, on what grounds should it be permissible?*

We do not have a view on whether a DTF that exercises discretion should be permitted to limit access to its facility. However, more generally, all DTFs should have some grounds for limiting trading access to certain types of participants in order to ensure the integrity of the transactions that take place on the DTF's system. For example, in the US, a swap execution facility has to ensure that every participant is an eligible contract participant, i.e., a sophisticated investor. A DTF should be permitted to restrict trading access to those types of sophisticated investors. Since most derivatives trading is institutional, DTFs should be permitted to refuse access to retail investors. However, we acknowledge that similarly situated groups of participants that meet prescribed sophistication or asset thresholds should be treated the same and benefit from the same access rights.

*12. Are the proposed organizational and governance requirements for DTFs appropriate? Are there additional organizational and governance requirements that the Committee should consider?*

Most of the proposed organizational and governance requirements for DTFs are appropriate. However, we recommend that the Committee place reasonable limits on any transparency requirements. Any requirements for a DTF to make public disclosure (such as on a website) of order execution process, access requirements or technology requirements should be limited so as to not require DTFs to disclose any commercially sensitive confidential information. Also, with respect to record keeping, we note that many jurisdictions in which foreign-based DTFs operate require records be kept for five years, not seven. In our view, future DTF rules should require records to be kept for five years and should permit records to be kept in various mediums, such as written records or voice recordings.

With respect to confidential treatment of trading information, we agree that DTFs should be prohibited from releasing a participant's order or trade information to a person other than the participant, a trade repository, the trading counterparty of the participant, other derivatives trading facilities, a securities regulatory authority or a regulation services provider without consent of the participant. There should also be allowance for information to be released to vendors that provide outsourcing services to DTFs without the need for participant consent, provided that any vendors that receive confidential information are under duties of confidentiality to the DTF.

*13. Is it appropriate that a DTF that does not exercise execution discretion be permitted to perform its regulatory and surveillance functions itself, or should it be required in all cases to engage a third-party regulation services provider for this purpose? Please explain.*

A DTF should be permitted to choose whether to perform its own regulatory or surveillance functions or engage a third-party regulation services provider. For smaller DTFs, the costs of engaging a third-party provider could be prohibitive and impact the commercial viability of the facility.

Also, if a Foreign-Based DTF uses a foreign-based third-party service provider to monitor compliance by participants with DTF rules and appropriately discipline participants in the event of non-compliance, the foreign-based third-party service provider should not require any authorization from Canadian regulatory authorities.

*16. Should pre-trade transparency requirements apply to OTC derivatives that trade on DTFs but that have not been mandated to be traded on DTFs? If yes, what requirements should apply, and should any exemptions be provided?*

In our view, pre-trade transparency requirements should not apply to OTC derivatives that trade on DTFs but that have not been mandated to be traded on DTFs. There are many options for price discovery in the market, such as bulletin boards, single dealer pages and RFQ facilities. Also, certain swaps trade infrequently and a pre-trade transparency requirement for such swaps may preclude maintaining confidentiality, thus adversely affecting the price to the customer. Pre-trade transparency requirements could significantly raise transaction costs for end-users with little benefit to price discovery.

*17. Are the proposed post-trade transparency requirements (involving real-time trade reporting as well as public reporting of certain daily data) appropriate for DTFs?*

If it is decided that a DTF will be required to report to a trade repository, then the DTF should be permitted to choose the trade repository to which it chooses to report.

Since 2013, Canadian derivatives market participants have made significant investments of time and resources to develop systems for reporting derivatives transactions in Canada. These systems are based on a reporting counterparty waterfall that involves only clearing agencies, dealer counterparties, Canadian financial institution counterparties and non-dealer counterparties. If that reporting waterfall were to be amended to include DTFs, all market participants would need to undertake costly reporting system modifications. We therefore recommend that the Committee consult with market participants and DTFs as part of a cost/benefit exercise to determine whether DTF reporting to trade repositories would be worthwhile. For DTFs, there would be a significant cost to collect jurisdiction information (such as guaranteed affiliate information) from its participants for reporting purposes and code that information into trade reporting systems. These costs could be avoided if the Committee preserves the status quo in Canada and doesn't require DTF reporting to trade repositories.

*18. What is the preferred method for real-time public reporting of transactions executed on a DTF (i.e., directly by a DTF, via trade repositories, or some other method)? What are the advantages and disadvantages of the proposed options?*

See comments above in response to question 17.

*19. When should deferred publication of trade information be permitted? Are there circumstances other than block trades?*

There should be exceptions from real-time public reporting by DTFs for block trades.

*20. Assuming that deferred publication of trade information should be permitted for block trades, what criteria should be considered when determining the minimum block trade threshold size to permit deferred trade disclosure?*

Canadian regulators should attempt to harmonize block trade threshold sizes with international standards whenever possible. This would mean that if deferred publication is permitted for a block trade in the United States or another comparable jurisdiction, then deferred publication of the block trade should be permitted in Canada.

*23. Are the proposed criteria for determining whether a derivative will be subject to a DTF-trading mandate appropriate? Should other criteria be considered?*

We agree with the criteria for determining whether a derivative should be subject to a DTF trading mandate, however we caution that some criteria should carry more weight than others. In particular, if there is no mandate for trading a particular derivative in the United States then there would be significant obstacles to making the derivative subject to a Canadian DTF-trading mandate. Cross-border flow and activity should be carefully studied prior to making any derivatives subject to a Canadian DTF-trading mandate.

Canadian market liquidity could evaporate if US counterparties are resistant to a DTF-trading mandate when trading with a Canadian counterparty.

*25. Are there any situations in which a product that has been mandated to trade exclusively on a DTF should be permitted to trade other than on a DTF? Should any category of market participants be exempt from a trading mandate?*

Commercial end-users should be exempt from the trading mandate.

*29. Is it appropriate to limit trading in OTC derivatives that have been mandated to be traded on a DTF to specific permitted execution methods, e.g., an order book, or a request-for-quote system offered in conjunction with an order book? Why or why not? If so, which modes of execution should be permitted for products that are mandated to trade on a DTF? Can an appropriate level of pre-trade transparency be achieved with other methods of execution? What other factors should be considered?*

It is not appropriate to require specific execution methods for the OTC derivatives that have been mandated to be traded on a DTF. Participants should not be restricted in their execution methods and must be able to use their expertise to determine how to execute their orders. Also, we agree with the proposal to allow market participants to enter into pre-arranged transactions that have been mandated-to-trade and then ‘expose’ those transactions to the market.

*30. What additional requirements should apply to DTFs with respect to trading in products that have been mandated to trade on a DTF?*

DTFs, whether authorized or exempt from authorization, should not be required to trade products that have been mandated to trade on a DTF. For example, it would not be appropriate to require a DTF that specializes in commodity derivatives to trade interest rate swaps, or a DTF that specializes in security-based swaps to trade currency swaps.

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Thank you for the opportunity to comment on the Consultation Paper. We would be pleased to discuss our thoughts with you further. If you have any questions or comments, please contact Blair Wiley (416.862.5989 or [bwiley@osler.com](mailto:bwiley@osler.com)).

Yours very truly,

***Osler, Hoskin & Harcourt LLP***